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Supreme Court, U.S.
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No. 01-422

IN THE

Supreme Court of the United States

SCOTT KAYSER D/B/A QUALITY EXPRESS,

Petitioner,

v.

ROADWAY PACKAGE SYSTEM, INCORPORATED,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

REPLY BRIEF FOR THE PETITIONER

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INTRODUCTION

Respondent's entire Opposition proceeds from the same erroneous assumption on which the decision below is based: that the FAA's procedural provisions somehow represent the preferred "default rules" that should apply whenever there is ambiguity about the parties' intended choice of law. As explained in the Petition, that assumption cannot be reconciled with the limited purpose Congress sought to achieve when it enacted the FAA. The FAA was designed only to "overrule the judiciary's long-standing refusal to enforce agreements to arbitrate," and to "place such agreements upon the same footing as other contracts." *Volt Info. Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 478 (1989) (internal quotation marks omitted). Congress never intended the FAA to provide a comprehensive set of procedural rules governing the arbitral process under every agreement "involving commerce," 9 U.S.C. § 2, for "[t]here is no federal policy favoring arbitration under a certain set of procedural rules." *Volt*, 489 U.S. at 476.

The Third Circuit, like other courts of appeals in the wake of *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52 (1995), has nonetheless created a presumption that the FAA should apply to the exclusion of state arbitration law unless there is extrinsic evidence demonstrating that the parties intended otherwise. There is nothing in the FAA, or in any of this Court's decisions interpreting the FAA, that authorizes the creation of such a presumption. Respondent predictably attempts to minimize the significance of the decision below by characterizing it as involving an issue "solely of contract construction" on which "there is no direct split of authority." Br. in Opp. 4, 13. That characterization, however, is contradicted by both the majority and concurring opinions below. Pet. App. 2a, 38a n.7. As Chief Judge Becker explained, the question presented is one of two

questions in this case that are "currently the subject of circuit-splits" and are "of considerable significance for the law governing arbitration." *Id.* at 2a.[†] Review is plainly warranted.

RESPONDENT OFFERS NO SUBSTANTIVE RESPONSE TO THE REASONS FOR GRANTING REVIEW SET FORTH IN THE PETITION.

1. There is no dispute that, with the decision below, seven circuits have now invoked *Mastrobuono* and distinguished *Volt* in interpreting arbitration agreements with general choice-of-law clauses against application of state arbitration laws and in favor of FAA arbitration rules. Br. in Opp. 12. As respondent candidly admits, this group represents "the *majority* of circuit courts to have independently examined the issue." *Ibid.* (emphasis added). Both the D.C. Circuit and the Fifth Circuit have invoked *Volt* to interpret general choice-of-law clauses in agreements subject to the FAA to incorporate state arbitration rules. Pet. 10, 15-16 (citing *Ekstrom v. Value Health, Inc.*, 68 F.3d 1391 (D.C. Cir. 1995), and *ASW Allstate Painting & Constr. Co. v. Lexington Ins. Co.*, 188 F.3d 307 (5th Cir. 1999)).

Respondent's only objection is that *Ekstrom* and *ASW* do not explicitly cite *Mastrobuono*. Br. in Opp. 13. This cannot reasonably be taken as a sign that the D.C. and Fifth Circuits ignored that decision or ruled without the benefit of its reasoning: both *Ekstrom* and *ASW* were argued *and* decided after *Mastrobuono* was handed down. Indeed, the Fifth

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[†] Respondent asserts that this case does not present "[t]he issue of whether contracting parties may choose to opt out of the FAA's standards for vacatur." Br. in Opp. 5 n.3. But, as explained in the Petition (Pet. 7 n.1), the Court must also address this subsidiary issue if it grants review, since that issue is antecedent to the question whether the agreement here in fact incorporates Pennsylvania's standard for vacatur. Like the question presented, this opt-out issue has divided the courts of appeals. Pet. 6-7; Pet. App. 2a, 10a-11a & n.3.

Circuit issued *ASW* more than four years after this Court handed down its decision in *Mastrobuono*, and in the wake of at least six decisions by sister circuits explicitly addressing the relationship between *Mastrobuono* and *Volt*. Pet. 16 (collecting cases).

The exclusive reliance placed by *Ekstrom* and *ASW* on *Volt* merely reflects the D.C. and Fifth Circuits' conviction that *Volt*, and not *Mastrobuono*, controlled the interpretation of the agreements at issue. On this point, *Ekstrom* and *ASW* are plainly correct. Like the California arbitration rule at issue in *Volt*, the state arbitration laws at issue in *Ekstrom* and *ASW* in no way undermined the federal policy of "ensur[ing] the enforceability, according to their terms, of private agreements to arbitrate." *Volt*, 489 U.S. at 476. *ASW* centered around a Texas statute that required courts to decide summarily challenges to the existence of an arbitration agreement. *See* 188 F.3d at 311. Because such challenges are properly resolved by courts under the FAA, *see Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 403-04 (1967), the Texas law not only was consistent with the FAA, but also furthered its pro-arbitration policy by expediting the process for enforcing valid arbitration agreements. Similarly, the Connecticut law applied in *Ekstrom* "surely d[id] not conflict with the FAA's primary purpose," 68 F.3d at 1396, since it imposed a *shorter* period within which to challenge an arbitration award than that prescribed by the FAA.

As explained in the Petition (Pet. 15-17), the reasoning employed by the D.C. and Fifth Circuits is irreparably at odds with the approach adopted by the circuits on the other side of the split. Those circuits have read *Mastrobuono* to preclude any construction of agreements with general choice-of-law clauses and arbitration provisions that incorporates state arbitration laws. *See PaineWebber Inc. v. Elahi*, 87 F.3d 589, 592-94 (1st Cir. 1996); *National Union Fire Ins. Co. v. Belco Petroleum Corp.*, 88 F.3d 129, 133-35 (2d Cir. 1996); *Porter Hayden Co. v. Century Indem. Co.*, 136 F.3d 380, 382-83 (4th

Cir. 1998); *Ferro Corp. v. Garrison Indus., Inc.*, 142 F.3d 926, 933-38 (6th Cir. 1998); *UHC Mgmt. Co. v. Computer Sciences Corp.*, 148 F.3d 992, 995-97 (8th Cir. 1998); *Wolsey, Ltd. v. Foodmaker, Inc.*, 144 F.3d 1205, 1209-13 (9th Cir. 1998). This rigid interpretation of *Mastrobuono* has been applied even in circumstances where, as in *Volt*, there was no conflict between the FAA and the state arbitration law at issue. *See, e.g., Wolsey*, 144 F.3d at 1213 (reading *Mastrobuono* to "dictate[]" that a general choice-of-law clause could not be read to incorporate the same California statute deemed by *Volt* to be consistent with the FAA). This approach is highlighted by the decision below, which construed a general choice-of-law clause against application of a state standard for vacating arbitration awards that is more deferential to arbitrators than the FAA's default standard. Pet. App. 8a n.2.

Respondent fails utterly to address the confusion in the circuits regarding the relationship between federal arbitration policy and state arbitration laws. Nor does respondent contest that the circuits are in disarray over the role of state *contract* law in interpreting arbitration agreements containing general choice-of-law clauses. This court has made clear that courts must apply state principles of contract interpretation when construing arbitration agreements. *See First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 944 (1995). Yet, courts interpreting such agreements have taken a variety of different approaches to state contract law, from indiscriminately invoking the New York and Illinois principles of contract interpretation applied in *Mastrobuono*, *see Ferro*, 142 F.3d at 937; *Chiron Corp. v. Ortho Diagnostic Sys., Inc.*, 207 F.3d 1126, 1130-31 (9th Cir. 2000), to ignoring state contract principles altogether, *see Porter Hayden*, 136 F.3d at 382-83; *UHC*, 148 F.3d at 996. Again, the Third Circuit's ruling exacerbates this confusion, interpreting the agreement in this case with absolutely no regard for state principles of contract interpretation. Pet. App. 16a-20a.

The division among the circuits on the question presented warrants this Court's immediate intervention.

2. Respondent asserts it "is not apparent" that the decision below "will have broad application," since contracting parties can freely "draft their agreement to avoid the problem the court faced here." Br. in Opp. 9, 8. This contention is belied, however, by the persistent recurrence of this problem in the courts.

If, as respondent maintains, contracting parties were readily able to draft agreements specifying whether state arbitration rules apply, this case and the many like it would never have arisen. *Mastrobuono* would have alerted private parties to the risks and uncertainty of using general choice-of-law clauses in arbitration agreements, and, on respondent's theory, would have driven them to draft with greater precision. Of course, *Mastrobuono* has *not* had this effect. In the six years since that decision was handed down, nine circuits have had to confront and interpret general choice-of-law provisions in agreements subject to the FAA. The published decisions by these circuits demonstrate clearly that parties continue to rely widely on general choice-of-law clauses, and courts continue to be confused about how to interpret them.

Respondent's suggestion that the decision below is unworthy of review because it merely announces a "limited rule of contract construction" (Br. in Opp. 11), is frivolous. The question presented is, in principle, no different from the issue of "contract construction" taken and reviewed by this Court in *Mastrobuono*. *See* 514 U.S. at 58 (explaining that "the case before us comes down to what the contract has to say"). Indeed, the confusion engendered by *Mastrobuono* itself makes the need for review here more urgent than it was in that case.

3. Respondent also attempts to minimize the significance of the Third Circuit's ruling by arguing that it neither

preempts state law nor expands the scope of federal law. Br. in Opp. 4-7. Respondent concedes, as it must, that the new "default rule of contract construction" adopted by the Third Circuit barred the application of Pennsylvania's vacatur standard in this case. *Id.* at 7, 9-10. It nevertheless maintains that the decision below does not operate with the force of preemption because it addresses a question "solely of contract construction." *Id.* at 4. As the Petition explains, this interpretation fails. Pet. 17-27.

It is telling that respondent nowhere identifies the source of authority for the new "contract construction" rule it concedes was adopted by the Third Circuit. The decision below makes clear that the new rule is one of substantive federal law, its source the Third Circuit's interpretation of FAA policy. After concluding that the general choice-of-law clause did not evince a clear intent to incorporate Pennsylvania's default standard, the Third Circuit adopted "a default rule" for interpreting agreements containing such clauses. Pet. App. 17a. Although this is a diversity case, the Third Circuit did not ground its new "default rule" in state law. *Id.* at 17a-19a. Rather, it explicitly held that its rule was dictated by "the FAA's history," the statute's "raison d'etre," and "*Mastrobuono*'s holding." *Ibid.* By the Third Circuit's own reckoning, then, its new default rule was driven by federal arbitration policy.

Respondent's suggestion that this rule cannot operate to preempt state law because it is "solely" a rule of contract construction reflects a fundamental misunderstanding of both preemption and the FAA. The purpose of the FAA is to ensure the enforceability of arbitration agreements, and to place such agreements "upon the same footing as other contracts." *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 219 (1985) (quoting H.R. Rep. No. 96, 68th Cong., 1st Sess., 1 (1924)). To effect this purpose, the statute "create[s] a body of federal substantive law of arbitrability . . . enforceable in both state and federal courts." *Perry v. Thomas*, 482 U.S.

483, 489 (1987) (citations and internal quotations omitted). This body of law takes the form not only of substantive principles governing the validity and enforcement of arbitration agreements, but also of background principles and presumptions that inform the manner in which arbitration agreements are interpreted. *See Moses H. Cone Mem. Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983) ("The Arbitration Act establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability."); *First Options*, 514 U.S. at 944-45 (explaining that the presumption in favor of arbitrability is reversed with respect to the question of who should decide arbitrability).

Like any other principle of contract interpretation predicated upon the FAA, the bright-line "contract construction" rule adopted by the Third Circuit has the force of substantive federal law. And it is precisely for this reason that the decision below threatens to create confusion regarding the proper scope of FAA preemption. Respondent insists that the Third Circuit's rule "does not expand the scope of federal law." Br. in Opp. 4. Yet, as this case amply demonstrates, this rule applies to bar the application of state law even when it in no way threatens the FAA's pro-arbitration policy.

Under the Third Circuit's default rule, any contract with both a general choice-of-law clause and an arbitration clause categorically must be read against application of state arbitration rules. Pet. App. 17a. It matters not that state contract principles of interpretation may indicate that the parties intended to adopt state arbitration rules. It matters not that the state arbitration rules at issue may be consistent with or even advance federal arbitration policy. Under the Third Circuit's new rule, the "FAA's history," its "raison d'etre," and "*Mastrobuono*'s holding" all compel the application of

FAA default rules in this instance, irrespective of whether federal arbitration policy is actually at stake.

That is a striking departure from this Court's FAA decisions, and, if permitted to stand, would risk a senseless expansion of FAA preemption. Time and again, this Court has explained that the FAA was not intended to occupy the field of arbitration law, *see Volt*, 489 U.S. at 477, but instead was intended only to safeguard the validity and enforceability of arbitration agreements, *see Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth*, 473 U.S. 614, 625 (1985) (explaining that the federal policy underlying the FAA "is at bottom a policy guaranteeing the enforcement of private contractual arrangements"); *Southland Corp. v. Keating*, 465 U.S. 1, 16 (1984). Accordingly, this Court has held preempted only "state legislative attempts to undercut the enforceability of arbitration agreements" *in toto* or as to particular claims. *Ibid. See, e.g., Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 687 (1996) ("Congress precluded states from singling out arbitration provisions for suspect status"); *Perry*, 482 U.S. at 491 (explaining that the FAA was "in unmistakable conflict with California's . . . requirement that litigants be provided a judicial forum for resolving wage disputes"). This policy is not offended by state laws that, like Pennsylvania's vacatur standard, enforce arbitration agreements with vigor comparable to or greater than the FAA.

As much as respondent would like to characterize the ruling below as a run-of-the-mill act of contract interpretation, the new rule it announces has significant implications for federal arbitration policy. This Court should grant review in order to rein in the Third Circuit, as well as other circuits that have given federal arbitration policy excessively broad reach.

4. Respondent's contention that "the decision below is in accord with both *Volt* and *Mastrobuono*" (Br. in Opp. 17), is wrong as well. Both of those decisions recognized that federal arbitration policy focuses on the validity and enforceability of arbitration agreements. *See* Pet. 19-20. *Volt*

held that the FAA did not preclude a construction of the general choice-of-law clause at issue as incorporating California's law providing for stays of arbitration because it did not undermine the statute's pro-arbitration policy. *See* 489 U.S. at 476; *accord Ferro*, 142 F.3d at 934 ("*Volt* did not present a situation in which state and federal law were in conflict."). *Mastrobuono* held that the New York arbitration law at issue did violate federal arbitration policy because it made certain issues non-arbitrable. *See Mastrobuono*, 514 U.S. at 62. In eschewing any particularized inquiry into whether Pennsylvania's deferential vacatur standard implicated the FAA's enforceability concerns, the decision below fundamentally misapplies federal arbitration policy as delimited by *Volt* and *Mastrobuono*.

Respondent insists that *Volt* is distinguishable based solely upon its deference to the state court's interpretation of California law. Br. in Opp. 17. But this point only underscores the need for clarification of the relationship between *Volt* and *Mastrobuono*. Following *Mastrobuono*, several circuits have relegated *Volt* to instances involving federal review of state-court decisions interpreting arbitration agreements. *See, e.g., Wolsey*, 144 F.3d at 1212-13; *Chiron*, 207 F.3d at 1131; *Ferro*, 142 F.3d at 935; *Porter Hayden*, 136 F.3d at 383 n.6; *Elahi*, 87 F.3d at 594 n.5; *National Union*, 88 F.3d at 134. The notion, however, that *Volt*'s holding was a function of the Court's deference to the lower state court's contract interpretation has been strongly criticized. *See, e.g.*, Paul D. Carrington & Paul H. Haagen, *Contract and Jurisdiction*, 1996 Sup. Ct. Rev. 331, 394 (suggesting that *Mastrobuono* distinguished *Volt* "perhaps somewhat disingenuously"); Thomas A. Diamond, *Choice of Law Clauses and Their Preemptive Effect on the Federal Arbitration Act: Reconciling the Supreme Court With Itself*, 39 Ariz. L. Rev. 35, 56-68 (1997). And, again, both the D.C. and Fifth Circuits have held that *Volt*'s reasoning has broader application.

5. Finally, respondent suggests that this case is an inappropriate vehicle for resolving the question presented because there is no relevant difference between Pennsylvania law and FAA law. As explained in the Petition (Pet. 10 n.2), this argument presents no obstacle to review of the Third Circuit's decision. This case comes to the Court on the assumption, made by both courts below, that the difference between the vacatur standard under Pennsylvania law and the FAA would be outcome determinative here. Pet. App. 9a n.2 (acknowledging that Pennsylvania's vacatur standard is "much narrower" than the FAA's, and that as a result "the choice of standards . . . could well be dispositive in this case"); *see also id.* at 48a. Thus, as is often the case, reversal by this Court would simply result in a remand to the Court of Appeals so that it (or perhaps the District Court) could reconsider in the first instance the propriety of the arbitrator's award under the correct legal standard supplied by Pennsylvania law.

CONCLUSION

For the reasons stated above and in the Petition, the Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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